Bundesvereinigung der kommunalen Spitzenverbände

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Opinion of the Associations of German Local Governments on the Commission's Non-Paper "Revised interpretative guidelines concerning Regulation (EC) No 1370/2007"

Ladies and Gentlemen,

thank you very much for the opportunity to comment on the EU Commission's draft for a revision of the interpretation guidelines for Regulation (EC) No. 1370/2007. We see a fundamental need for revision of the draft, as you can see from the detailed comments. We would be grateful when these points were considered before adopting these guidelines. We would be happy to answer any further questions you may have.

Kind regards

[redacted]

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Opinion of the Associations of German Local Governments

on the

Commission's Non-Paper "Revised interpretative guidelines concerning Regulation (EC) No 1370/2007 on public passenger transport services by rail and by road"

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We strongly support the joint position of the CEMR on the non-paper submitted by the EU Commission for a revision of the interpretative guidelines for Regulation (EC) No. 1370/2007. Since we also have comments in addition to this opinion (see Points 2.2.6. and 2.3.1), we sent you our opinion additionally. The additional points are highlighted in yellow.

Basic remarks

Regulation (EC) No 1370/2007 is of central importance in Europe for the award of public transport services by rail and road.

As umbrella organisations of local governments in Germany, we advocate the interests of local competent authorities that are responsible for planning, organising and financing local public transport and, in doing so, are governed by the legal provisions of the regulation.

We welcome the intention of the Commission to adapt the guidelines to the amendments of the Fourth Railway Package and the more recent case law of the European Courts. Even though interpretative communications of the Commission are not legally binding in a strict sense, they have high legal significance. They are part of the Union's soft law and they may be considered as recommendations that have to be taken into account. In any case, they have a high de facto relevance for legal practice.

However, from the perspective of competent local authorities, the Commission's draft guidelines are a cause for considerable concern, especially with regard to achieving European and national climate protection goals. Contrary to the Commission's own objective to shift more traffic to climate-friendly modes of transport, the draft guidelines would introduce new restrictions to public service obligations and thereby considerably impede and jeopardize the extension of local public transport services that are necessary to achieve the climate goals.

Furthermore, some of the Commission's comments, in our view, are not covered by the legal provisions of Regulation (EC) No 1370/2007 and would significantly change its requirements. We consider this to be legally questionable and beyond the powers of the Commission (ultra vires).

In some parts, the revised guidelines seem to contradict the concept of Regulation (EC) No 1370/2007. The Regulation is based on the concept that public service obligations are indispensable to enable a higher quality of local transport services in the Member States (see for example, recitals 3,

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9, 13, 17, 27, 28, 33, Article 2 e and Article 2 a). In our view, this basic decision must not be called into question or even be reversed by additional bureaucratic hurdles and additional obligations to provide evidence (e.g. for a “real need” of public services). Necessary extensions of local passenger transport services, which are needed and supported by all political levels, would be made more difficult or could be legally jeopardized or even be prevented.

A central objective of the regulation is the control of state aid and the prevention of overcompensation. This is ensured in particular by the instrument of public tendering. Tendering procedures guarantee market prices and prevent overcompensation. The Commissions revised guidelines would undermine this basic principle and try to introduce new formal and procedural requirements that precede the actual public tendering procedure and the decision on the award of public contracts (in particular 2.2.3, 2.4.1, 2.5.3, 2.5.4). Especially by introducing these new procedural requirements, the draft guidelines go beyond the wording of Regulation (EC) No 1370/2007, and thus inadmissibly restrict the wide scope of assessment the Regulation expressly assigns to the competent local authorities. In addition, at various points in the draft, the guidelines draw conclusions from judgements of the EGC concerning ferry services in the Mediterranean. The market situation in ferry transport, however, may not be compared or transferred to local passenger transport by rail and road.

Detailed comments

Re 2.1.5 Article 1(2). Multimodal public service obligations

In the coming years, an increasing use of flexible forms of public passenger transport services is to be expected in order to ensure accessibility, especially in sparsely populated (peripheral or rural) areas and at off-peak times, in the sense of an adequate basic service (German: “Daseinsvorsorge”) and as part of an extended local public transport service. Therefore, it should be clarified in the guidelines that such forms of flexible on demand services can be part of a public service contract, as Regulation (EC) No 1370/2007 is, by no means, limited to line-bound transport services. In Germany, for example, the Passenger Transport Act was recently amended. It now includes flexible, on demand transport services as an integral part of public transport services (with reliable times of service, tariffs and transport obligations). In the German Passenger Transport Act such services are therefore treated like classic regular services and, as such, are also subject to the regime of Regulation (EC) No 1370/2007. In our view, this could also be a suitable reference at European level.

Re 2.2.3. Article 2 point (e) and Article 2a. Definition of the nature and extent of public service obligations and of the scope of public service contracts

We consider the comments under 2.2.3 as particularly problematic. They impose a number of restrictions to the use of public service obligations. On the one hand, the Commission emphasizes the wide margin of appreciation when Member States define services of general economic interest. At the same time, however, the Commission demands that a number of additional requirements must be met, adding that any deviation from these new procedural requirements could jeopardize the whole award procedure.

In addition to the Commisson's comments on its power to call into question the specifications of a public service obligation in the case of a ‘*manifest error*’, the Commission points to the fact that the Member State's power to define a service of general economic interest is not unlimited and, furthermore, that the definition of a service of general economic interest must not be exercised arbitrarily and for the sole purpose of circumventing competition rules. We consider this basic remark as inappropriate:

We would like to point out, that there is no attempt to circumvent the rules of competition, as the Commission insinuates, when applying the provisions of Regulation (EC) No 1370/2007, because

these are the relevant rules of competition. By applying these rules, competition is enabled, not circumvented. Therefore, the Commission should abstain from these remarks and from putting member states, competent authorities and the whole sector under general suspicion.

a) Public transport policy documents

According to the draft, public service obligations must be consistent with the '*Member States' public transport policy documents'*. However, this does not correspond with the wording of Article 2a of the Regulation, which speaks of policy documents '*in the member states'*, not "of" the Member States.

Here, as elsewhere in the revised guidelines, the level of the Member states and the level of the local competent authorities get mixed-up. It is our strong opinion that the need for public transport services can be assessed reliably only at a regional and local level, and stakeholder participation – in a meaningful way - can be organised only there. Therefore, regional and local transport concepts and plans should be the rule.

Article 2 a paragraph 1 subparagraph 4 clearly leaves the content and format of public transport policy documents and the procedural arrangements to the Member States.

Therefore, there is no need for further interpretative comments on the part of the Commission. The guidelines need to clarify only that regional and local transport concepts and plans are and can be the relevant framework of reference within the meaning of Article 2a. Thus, the Commission should limit itself to a non-exclusive list of examples of policy documents in question, based on the actual practice in the Member States.

Remark before letters b) to f)

From a discussion with representatives of the Commission, for which we are sincerely thankful, we learned that headings and respectively subparagraphs to Re 2.2.3 (here commented under letters b to f) are meant to be part of a so-called SNCM check (with reference to judgment T-454/13). However, the Commission's explanations have not diminished our concern.

The proposed SNCM test is in our opinion not derived transparently in the proposal, it is in the actual draft not comprehensible and the application of the proposed test levels to different land transport types is not properly shown (e.g. heavy rail, cross-border traffic, long distance relations; not: light rail, local transport, even when cross border).

The introduction of such an extensive test procedure only seems appropriate if all options for determining the required level of public service obligations are listed in stage 1 (here letter b: need for public service contracts); so far, the draft names only one misleading example (user demand). Furthermore, local transport (in Germany defined as connections less than 50 km or travel time less than 1 hour) would have to be consistently excluded from levels 2 ff. (here letter c ff.). This could be seen as a "de minimis" clause to avoid excessive testing and adverse effects on the tendering of local transport contracts. Furthermore, there is no "free market" for local transport throughout Europe, but a market consequently regulated according to Regulation (EC) No. 1370/2007, and so there is no need to add the SNCM test on these contracts for state aid reasons. The Regulation (EC) No. 1073/2009 could also provide arguments for the proposed distinction.

b) Existence of real need

According to the draft guidelines, there must be a '*real need*' for the public service requirements. However, the notion of "real need" is narrowed to '*user demand*', which, in addition, is to be assessed and determined by customer surveys. This is far too narrow and insufficient and unsuitable to define the required level of public service obligations. The assessment of the needed level of public service must not complicate the planning and organisation of public transport and must not restrict the

possibility to provide a level of service exceeding current demand. The level of service to be attained should be set by future-oriented local transport concepts (for which customer surveys may provide a basis but are only one of several possible aspects). In order to encourage people to switch to bus and rail for reasons of climate protection and for more livable cities and rural areas, a level of service must be provided that offers a better and more extended local public transport than before to represent an attractive and viable alternative to less sustainable transport modes. In a strict interpretation of the Commission's guidelines, this would not be admissible. Therefore, the guidelines need to be amended and clarified accordingly. In any case, the concept of a "real need" must include the creation of future user demand.

c) Examination of market failure

Furthermore, the Commission's revised guidelines require a '*market failure*' to be demonstrated in advance. In this regard, the Commission seems to demand some kind of "market investigation procedure".

However, Regulation (EC) No 1370/2007 views regulated competition ("competition for the market") as the general rule, while completely unregulated competition is seen as an exception.

In our view, a '*market failure*' within the meaning of the guidelines must be assumed in general and in all member states, because public transport in total does not cover costs. In this context, an examination of the market failure '*for each route*', as apparently required by the Commission, contradicts the explicit provisions of the Regulation. It would be diametrically opposed to the possibility of grouping cost-covering and non-cost-covering services as explicitly permitted and desired by the regulation. It would invite cherry picking and would require an inefficient use of public subsidies.

For the reasons mentioned above, we strictly reject a more elaborate market investigation procedure, especially with regard to individual routes.

d) No legal preference for the adoption of general rules

The Commission considers that, when choosing public service obligations, the one that is the least harmful approach to the internal market should be chosen. In this regard, the Commission states as an example that a general rule should be adopted instead of awarding a public service contract. However, this is highly problematic: A general rule has a much more limited range of application. It can only be used to compensate for maximum tariff requirements. Therefore, a general rule cannot generally be regarded as an equally suitable, milder means. It just cannot be equated with a public service contract. Regulation (EC) No 1370/2007 therefore views the award of a public service contract as the general rule and regards the adoption of general rules only as an exception. Thus, there is no legal preference for general rules. Accordingly, the third sentence of Article 3 paragraph 2 of the regulation explicitly clarifies that even when compensating maximum tariff requirements this may be done as well by a public service contract.

e) Possibility to group cost-covering and non-cost-covering services in the public service contract

Article 2a of Regulation (EC) No 1370/2007 explicitly grants the possibility to group cost-covering and non-cost-covering services. Although the draft guidelines refer to this provision, the further comments of the Commission immediately restrict this possibility by again referring to the "real need of the public service" ('*The grouping of cost-covering and non-covering services must be necessary and proportional to the objective of fulfilling a real need for public service.*') and by stating that the grouping

must serve the goal of a “coherent transport system” and of “reaping the benefits of positive network effects” rather than “only limiting the amount of compensation”.

However, this differentiation appears theoretical and creates legal uncertainties for the formation of local transport networks. It is not possible to clearly distinguish in an objective way when the creation of a network serves to ensure a coherent transport system and when it serves only to reduce the need for public subsidies. Both aspects will regularly (and quite naturally) go hand in hand. In addition and above all, there is no legal basis for the Commission's view that grouping is inadmissible on the grounds of minimising subsidy requirements. This interpretation cannot be derived from the regulation and therefore needs to be amended.

f) Invalidity of public service contracts in the event of infringement of the requirements

Last, and not least problematic, the Commission holds the view that a breach of the above procedural requirements makes the award of a public service contract inadmissible and invalid and would require a complete recovery of all grants. This would lead to hardly controllable legal and economic risks for the award of public transport services, especially as there is no time limit. Public service contracts, even when awarded in a public tendering, could be called in question even after many years. This is particularly problematic, as, in addition, the Commission's comments indicate no restriction to a ‘*manifest error*’. Rather, any violation of the procedural requirements seems to potentially and permanently call into question the awarded contracts.

We reject this view strongly as it would make it substantially more difficult or almost impossible to provide public transport services.

In view of their far-reaching and detrimental consequences, the Commission’s guidelines need to be reconsidered and amended. The assessment under State aid law must be limited to the question of overcompensation. There needs to be a broad discretion for the Member states. They must be able to exercise freely and without procedural restrictions, especially in view of climate policy objectives.

Furthermore, we would like to point out that a public tendering does not interfere with the fundamental freedoms of the European Single Market, as the Commission apparently believes. Quite to the contrary, the award of a public service contract under Regulation (EC) No 1370/2007 serves precisely to organise a market competition in accordance with the European Single Market. Thus, a public tendering is not a restriction of the European Single Market or its freedoms, but rather the securing and enablement of these freedoms.

The decision of the General Court in the SNCM case, on which the Commission relies to justify its restrictive procedural requirements, related to state subsidies for ferry services in the Mediterranean Sea. However, the facts of the case and the reasons for the decision cannot be transferred to public passenger transport in general. In contrast to ferry connections, public transport competes strongly with other mobility alternatives, especially with motorized individual transport. If the Commission and the member states want to shift traffic to more sustainable transport modes, public transport services must be especially attractive.

Furthermore, the reference to the SNCM case is not convincing from a legal point of view, neither. Regulation (EC) No 1370/2007 precludes a recourse to criterias comparable to the judgment of the ECJ in case Altmark Trans. On the other hand, the compensation granted in maritime transport is based on Article 106 (2) TFEU, whereas that in public transport is also based on Articles 91 and 93 TFEU.

The new interpretations in the draft guidelines would cause many legal uncertainties and make the already highly contentious tendering procedures even more vulnerable to legal actions. In order to ensure the award of public transport services and allow for a shift to more climate-friendly transport modes, the Commission’s guidelines need to be reconsidered and amended.

Re 2.2.6. Article 4(7) and Article 5(2)(e). Conditions of subcontracting

Article 5(2)(e) Regulation (EU) No 1370/2007 requires the internal operator to provide '*a major part*' of the public passenger transport service itself. As in the existing interpretative guidelines, the Commission continues to take the view that an internal operator must therefore provide at least two thirds of the transport service itself. It implies that a special justification is required for subcontracting more than 33%.

However, this limit is set arbitrarily. The wording of Article 5(2)(e) states that an internal operator must provide '*the major part*' of the passenger transport service itself. This can either be interpreted in relation to the transport service *as a whole* or – more narrowly – only in relation *to the parts of the service provided for* by other operators (i.e. subcontractors). In the first case, the execution of more than 50% of the transport service would already constitute the "bigger" (i.e. the major) part of the transport service and would thus be sufficient to meet the requirements of the Regulation. In the latter case, even less than 50% would be sufficient (for example, an internal operator performs 25 or 35% of the service itself, while a number of other operators (subcontractors) provide each between 5 and 10% of the service).

In no case, however, does the wording of the regulation support the Commission's exceedingly narrow interpretation that the internal operator needs to provide "at least two thirds" of the transport service itself. The Commission's interpretation would make sense if Article 5(2)(e) required internal operators to provide "by far the major part" of the service. However, this is not the case. Thus, the Commission's comments restrict unduly the possibility of subcontracting and need to be amended.

We would also like to point out that recital 19 of the Regulation has a much more favorable view of subcontracting by stating that "subcontracting can contribute to more efficient public passenger transport and makes it possible for undertakings, other than the public service operator which was granted the public service contract, to participate".

In our view,-subcontracting is indeed a good means of offering smaller companies a chance to become active on the market. It also enables the necessary flexibility in the short-term implementation of service extensions which are necessary to meet climate protection goals.

Therefore, pursuant to recital 19, the Commission's revised guidelines should make clear that the competent authorities, as laid out above, are assigned a much broader margin of appreciation to determine the modalities for subcontracting the case of services performed by an internal operator.

Re 2.3.1. Article 5a. Access to rail rolling stock

Regulation (EC) No 1370/2007 grants discretionary power to the competent authorities whether or not they decide to take measures to provide access to rail rolling stock. However, the draft guidelines unduly restrict this discretion by requiring competent authorities to carry out various checks. They require an assessment of the financial, technical or regulatory barriers, a suitability analysis of the available rolling stock and the early publication of a test report. Above all, the Commission threatens to cancel the award procedure if no action is taken despite a positive test report.

In this way, the Commission introduces an obligation to guarantee access to rolling stock through the back door. In contrast, the European Council had expressly rejected such an obligation in the legislative procedure for the Fourth Railway Package with reference to the possible negative effects on public budgets.

In addition, the Commission's comments on contract durations and extension options give cause for concern, as amortisation can often only be achieved through corresponding extensions of the contract duration. The rolling stock must also be available before the start of the contract period.

Therefore, in our view, the draft guidelines constitute an inadmissible deviation from the provisions of Regulation (EC) No 1370/2007. The clear provisions of the newly inserted Art. 5a must not be complicated and there must not be created bureaucratic hurdles for an essentially positive option to make rolling stock available.

Re 2.4.1 Article 5(2)(b). Conditions under which a public service contract may be directly awarded to an internal operator

The Commission takes the view that as a consequence of possible infringements of Article 5(2), a participation of an internal operator in a competitive tendering questions the validity of the direct award of a public service contract to that operator. The Commission refers to the opinion of the Advocate General in Joined Cases C-350/17 and C-351/17 (Mobit). However, the ECJ did not follow the opinion of the Advocate General.

In our view, the only consequence of the unlawful participation of an internal operator in a competitive tendering is that it must be excluded from the relevant (subsequent) tender. In contrast, a previously validly concluded direct award remains unaffected (pacta sunt servanda). The draft guidelines should be amended accordingly.

Re 2.5.3. Overcompensation – ex post checks and 2.5.4. The notion of 'reasonable profit' - here: application of the annex to competitively awarded transport contracts

In the above-mentioned sections, the Commission states several times that even if a public service contract has been awarded in a competitive tendering procedure, a subsequent overcompensation check must be carried out, which must also include a review of the public grants with regard to reasonable profit. In doing so, the Commission contradicts its own basic premise that a price arrived at in fair competition is to be considered an appropriate market price per se. The purpose of a competitive tendering is precisely to determine an appropriate market price.

Therefore, if all the transport services laid down in a public service contract have been carried out and the contract was fulfilled properly, the question of overcompensation or reasonable profit should not be raised again in hindsight. The guidelines should clarify this.

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